

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)

Price Cap Performance Review for)

Local Exchange Carriers;)

Treatment of Video Dialtone)

Services Under Price Cap Regulation)

CC Docket No. 94-1

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COMMENTS OF
SOUTHWESTERN BELL TELEPHONE COMPANY

Southwestern Bell Telephone Company (SWBT) hereby files its Comments on the Further Notice of Proposed Rulemaking (FNPRM) issued by the Commission on February 15, 1995.¹

I. VIDEO DIALTONE SERVICES SHOULD NOT BE SUBJECT TO PRICE CAP REGULATION.

In its FNPRM, the Commission tentatively concludes, on an extremely minimal record, that video dialtone (VDT) services should be subject to price cap regulation. SWBT believes that such a decision would fail to recognize the highly competitive nature of the existing video marketplace, particularly with respect to LEC entry as a VDT provider.

SWBT believes LEC provision of VDT should not be subject to price cap regulation. While VDT has yet to be offered to a single customer on a commercial basis, there are already several different types of providers of video services actively competing for customers in the "video marketplace." These providers include incumbent cable operators, Direct Broadcast Satellite (DBS)

¹ In the Matter of Price Cap Performance Review for Local Exchange Carriers; Treatment of Video Dialtone Services Under Price Cap Regulation, CC Docket No. 94-1, Further Notice of Proposed Rulemaking, (FCC 95-49) (released February 15, 1995) (FNPRM).

providers, wireless cable operators, and video rental retail outlets. It is incontrovertible that in this rapidly developing marketplace, competition itself is already fully capable of regulating the price of video services provided by LECs.

Furthermore, LECs will enter the video marketplace with no customers, and will be competing directly against the incumbent cable operators, which already have a substantial video market presence. Alternative sources of video programming, such as DBS and wireless cable, are already offering their service to the marketplace. Given all of these video distribution alternatives (already in the marketplace), there is simply no reason VDT services should be included in price cap regulation.

Finally, regulatory parity compels the conclusion that LECs' VDT services should not be subject to price cap regulation. The Commission has already recognized that VDT will "function as an effective competitor" to existing cable operators.² A fortiori, cable television must offer effective competition to VDT providers. Importantly, LEC VDT offerings would no doubt pass the test for "effective competition" under 47 U.S.C. 543(1) and would therefore be subject to streamlined regulation (i.e., not subject to price cap regulation). This fact alone should strongly suggest to the Commission that not subjecting VDT to price cap regulation would be good public policy and would represent equal treatment under the law.

² Report and Order, MM Docket 92-266, 8 FCC Rcd 5631 (Cable Rate Regulation Order), para. 21.

II. IF THE COMMISSION IMPOSES PRICE CAP REGULATION ON VIDEO DIALTONE SERVICES, A SEPARATE PRICE CAP BASKET MAY BE PROPER UNDER THE CIRCUMSTANCES.

In its FNPRM the Commission tentatively concludes that a "separate basket" is needed for VDT service. The Commission asserts that a separate price cap basket would "ensure that telephone ratepayers do not improperly subsidize video dialtone service," and that the technical and competitive characteristics of video dialtone are not similar to any services in our existing price cap baskets."³

As discussed above, SWBT does not believe the Commission has adequately analyzed or considered the competitiveness of the video marketplace. Nor has the Commission developed appropriate criteria for allowing the regulation of LEC-provided services subject to significant competition to be streamlined (i.e. removed from price cap regulation). If the Commission does adopt price cap regulation for VDT services, however, SWBT believes it should do so only as a temporary measure, and on such a basis, SWBT is willing to accept a separate basket for VDT service.

SWBT is generally opposed the creation of new baskets under price cap regulation when new services are offered. However, SWBT expects the Commission to carry through with its development of criteria for the assessment of the competitiveness of LEC services market that it noted in its LEC Price Cap Review Order.⁴

³ FNPRM at paras. 9, 11.

⁴ In the Matter of Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1 First Report and Order, (FCC 95-132) (released April 7, 1995) (LEC Price Cap Review Order) at para. 16.

When that assessment is completed, SWBT is confident that VDT will be removed from price cap regulation, as it ought to be now. The placement now of VDT in a separate basket will facilitate its removal.⁵ This treatment would be consistent with and analogous to the Commission's statement in the LEC Price Cap Review Order that it is prepared to remove LEC interexchange services from price cap regulation once it has appropriate transition rules in place, and the record demonstrates that services satisfy the relevant standards.

III. OTHER IMPLEMENTATION ISSUES MUST BE ADDRESSED.

A. The Commission Should Not Ignore Regulatory Parity When Setting The Productivity Factor For Video Dialtone.

In its FNPRM, the Commission declined to suggest a particular productivity factor for the proposed separate VDT basket. Instead, it asked parties to comment on the appropriate formula in light of the specifics regarding the LECs' provision of VDT service.⁶ The FNPRM noted that the LEC interexchange basket productivity factor differs from the factor that applies to the other LEC baskets, and that the Commission had recently declined to include a productivity offset in the price cap formula applicable to cable television rates.

On this issue as well, the Commission has the benefit of little, if any, actual evidence. There is no history regarding the

⁵ The FNPRM implies that technical characteristics of VDT may necessitate a separate basket. The technical characteristics of a service are not relevant to the form of price regulation, if any.

⁶ FNPRM at para. 16.

actual experience of LECs providing VDT and the related productivity. Thus, by necessity, the Commission must rely on other principles and approaches if it decides to apply a productivity offset to VDT.

SWBT recommends that the Commission strive to treat all providers of similar services equally. Assuming that VDT service should be subject to price cap regulation at all, (which it should not) the price cap regulation applied should strive to establish regulatory parity between LECs and other video service providers.

SWBT suggests that for an interim period, the Commission should adopt a productivity offset based on an average of the minimum productivity factor of 4.0% that was adopted in the LEC Price Cap Review Order,⁷ and the 0% productivity factor in the cable television price cap plan.⁸ The resulting interim productivity factor of 2.0% would provide a fair initial starting point subject to the eventual removal of VDT from price cap regulation. This approach could be analogous to the Commission's treatment of the productivity offset for the LECs' interexchange services.⁹ There is no need to be as precise with this factor since it should not be expected that VDT services will be explicitly price cap regulated for very long (perhaps not more than a year), and since competition in the video services market will

⁷ LEC Price Cap Review Order at para. 199.

⁸ In the Matter of Implementation of Sections of the Cable Television Consumer Protection Act of 1992 -- Rate Regulation, MM Docket No. 93-215, Memorandum Opinion and Order, FCC 94-226 (released September 29, 1994) at para. 7.

⁹ LEC Price Cap Review Order at para. 407.

most probably make "pricing to the cap" rare with the passage of time.

B. The Initial Cap Should Be Set Using The Existing Price Cap Rules For New Services.

The FNPRM tentatively concludes that the best approach to establish the initial rates would be to apply the existing rules for new services.¹⁰

SWBT disagrees with the Commission's specific refinement of the new services test for VDT,¹¹ but agrees that VDT be incorporated into the LEC price cap indexes using the existing new service method (but modified as described below). The existing rules provide an appropriate template to determine an initial Price Cap Index (PCI). Initialization of a VDT price cap index (PCI) and actual price cap index (API), each at 100, would be acceptable. However, since VDT would be the only service in the new basket, VDT could and should be brought in under price cap calculations and regulations at the effective date of the LEC's VDT tariff.

¹⁰ FNPRM at para. 18.

¹¹ In the Matter of Telephone Company - Cable Television Cross-Ownership Rules, Sections 63.54-63.58 and Amendments of Parts 32, 36, 61, 64 and 69 of the Commission's Rules to Establish and Implement Regulatory Procedures for Video Dialtone Service, CC Docket No. 87-266, Memorandum Opinion and Order on Reconsideration and Third Further Notice of Proposed Rulemaking, FCC 94-269 (released November 7, 1994) (VDT Recon. Order) at paras. 207-213. SWBT does not imply that the specific VDT new services support requirements that have been applied in this case are appropriate for this or other LEC new service offerings. SWBT has argued in the past and continues to believe that the current support requirements for new LEC services are overly burdensome and should be modified.

C. No Service Category Bands Should Be Imposed.

The Commission also requests comment on whether VDT service requires establishment of separate service categories in the tentative proposed separate video dialtone basket.¹²

SWBT proposes that no separate service categories be established at this time. As the Commission recognized in its VDT Recon. Order, the nascent VDT service market is too early in its development to warrant any explicit pricing constraints on rate elements.¹³ The rate elements for VDT are not well-defined because the effects of actual market demand on the structure of a LEC VDT service offering have not been experienced. Also, the expected means of provisioning VDT services do vary significantly. For the foreseeable future it is unlikely these conditions will change. At present, therefore, it is clearly premature to establish any but the most flexible price cap structure for VDT.

D. For An Interim Period, VDT Costs And Revenues Should Be Included In The Sharing And Low-End Adjustment Calculations.

In its FNPRM, the Commission seeks comment on whether the cost and revenues of video dialtone should be included in a LEC's interstate rate of return for purposes of calculating the sharing and low-end adjustments.¹⁴ The Commission has already concluded that "the sharing mechanism is not essential to ensuring that LEC

¹² FNPRM at para. 20.

¹³ VDT Recon. Order at para. 196.

¹⁴ FNPRM at para. 25.

rates under price cap regulation remain just and reasonable."¹⁵ The Commission also tentatively concluded that sharing and the low-end adjustment "should eventually be eliminated and we should move to a system of pure price caps."¹⁶

Obviously, by continuing earnings regulation, even for an interim period, significant dilemmas are created regarding how to apply an earnings sharing mechanism when LECs enter entirely new areas of business. The Commission already recognizes that the proper long-term answer is a pure price cap plan without any ties to earnings, as it regulates AT&T and cable TV providers today.

Also, to the extent that price cap LECs elect the highest productivity offset/no sharing option in the interim LEC price cap plan, concerns regarding the mechanics of price cap sharing are moot. As a result, there may be little need for any rules changes regarding sharing.

As with the selection of the appropriate productivity offset, SWBT's recommendation is that the Commission's treatment of VDT be analogous to its treatment of LEC interexchange services. Because, in the interim, the sharing and low-end adjustment mechanisms have not been eliminated for LECs providing VDT, VDT costs and revenues should be included in the general sharing and low-end adjustment calculations.

At this point, it would be inappropriate and wasteful to attempt to modify Part 36 and Part 69 rules to develop stopgap cost

¹⁵ LEC Price Cap Review Order, para. 16.

¹⁶ Id., para. 197.

allocation rules specifically for VDT. There would be little, if any, evidence on which to develop those rules, and doing so would only delay the introduction of VDT services.

The Commission has noted that sharing provides the ability and incentive for price cap LECs to cross-subsidize, and maintains the disadvantages of rate-of-return regulation. On this basis alone, SWBT urges the Commission to quickly move to eliminate sharing. However, if sharing continues, a contentious and protracted proceeding would be needed to separate VDT costs and revenues from the other portion of the calculations. This process is unnecessary in the competitive context of VDT.

IV. CONCLUSION

For the foregoing reasons, SWBT respectfully requests that the Commission adopt the recommendations detailed above.

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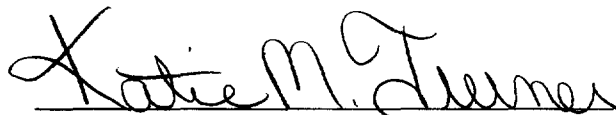
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CERTIFICATE OF SERVICE

I, Katie M. Turner, hereby certify that the foregoing, "Comments Of Southwestern Bell Telephone Company" in Docket No. 94-1, has been filed this 17th day of April, 1995 to the Parties of Record.

A handwritten signature in cursive script, reading "Katie M. Turner", written over a horizontal line.

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